



# The Executive Budget

FY 2010 and FY 2011  
Status and Recommendation

# Topics



## Budget Status

- What's the Problem?
- How did we get here?

## Budget Recommendations

- Principles
- Plan
- Budget Reform
- Immediate Actions

# What's the Problem?



There are three interconnected problems

- Current year deficit
- Structural deficit
- Cash flow

# What's the Problem?



## Current Year Deficit

- Current year deficit is anticipated to be \$1.4 billion
- \$480 million left over from FY 2009

The \$1.4 billion deficit is approximately:

- 46% of the General Fund revenues anticipated for the rest of the year
- 36% of the remaining General Fund appropriations for the fiscal year

# What's the Problem?



## Structural Deficit

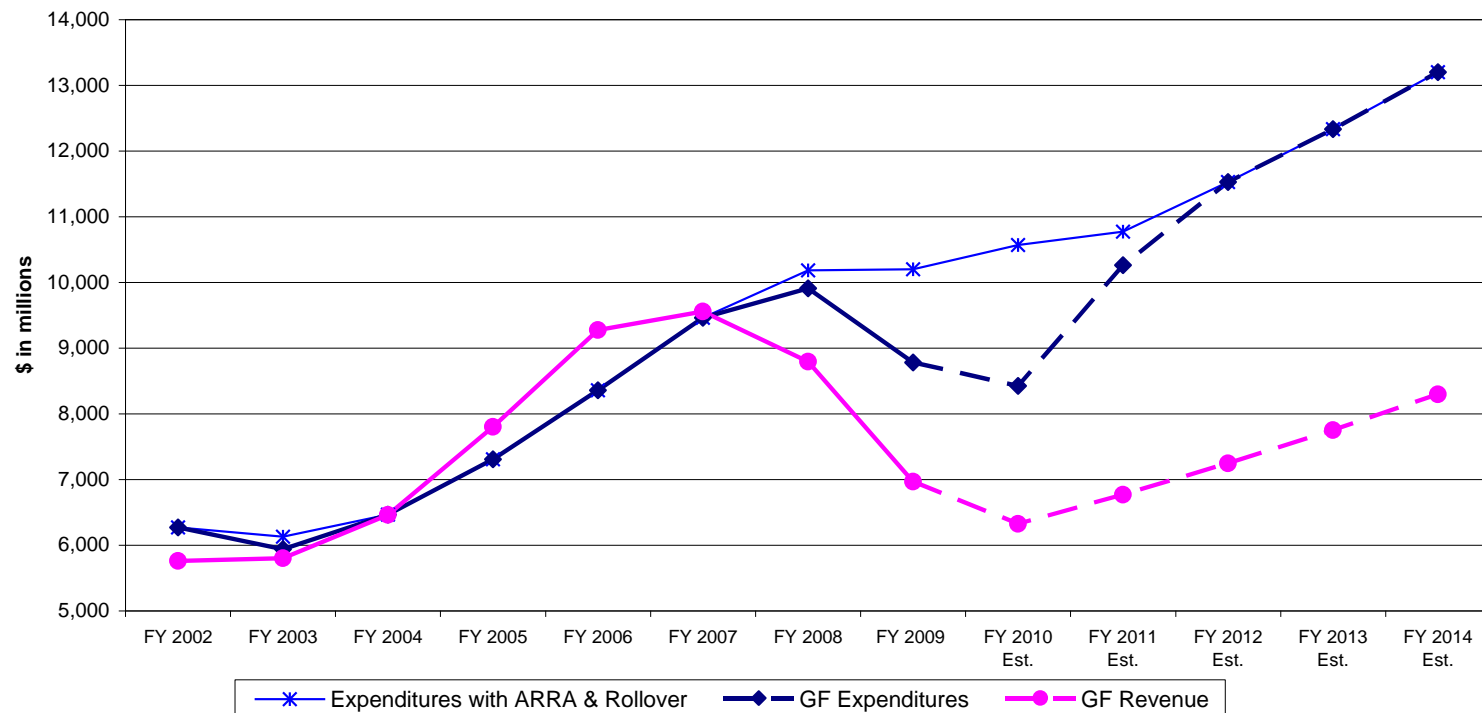
- Arizona has a structural deficit – our revenues and expenditures are out of alignment.
- This misalignment will produce a \$3.2 billion deficit in FY 2011.
- A \$3.2 billion deficit in FY 2011 amounts to:
  - 47% of anticipated General Fund revenues in FY 2011.
  - 33% of the General Fund “continuation” budget for FY 2011.

# What's the Problem?

## -Structural Deficit



General Fund Ongoing Revenue and Expenditures before Solutions



Assumptions: **Revenue:** Ongoing revenue does not include one time items such as fund transfer, asset sales, etc. Growth rates assumptions: FY10: -9.2%, FY11:7%, FY12 and 7%. **Expenditure:** Ongoing expenditure does not include rollover or ARRA. FY10 and FY11 estimated Expenditure from most current S&U, FY12 and beyond assuming 7% growth.

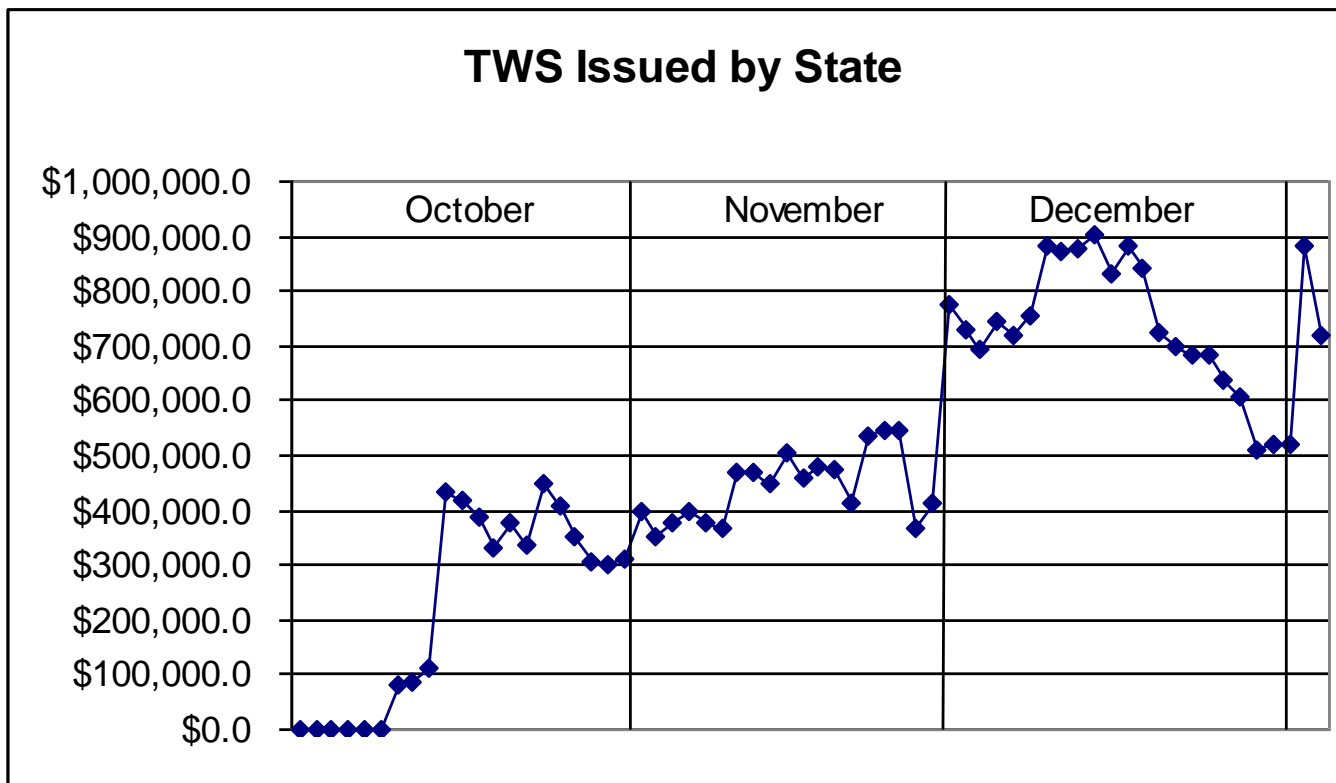
# What's the Problem?



## Cash Flow

- Every day the General Fund is borrowing every dollar of uncommitted state cash in the State's custody: approximately \$1.5 billion. The General Fund plus these uncommitted dollars are known as the Operating Fund.
- In addition, the State has created two facilities to borrow non state funds, an internal line of credit worth approximately \$500 million and an external line of credit with Bank of America worth \$700 million.
- Total available daily external credit of \$1.2 billion.
- Currently the State makes daily calculations to determine if the State has sufficient cash to cover expenses.

# Cash Flows





# Topics



## Budget Status

- What's the Problem?
- **How did we get here?**

## Budget Recommendations

- Principles
- Plan
- Budget Reform
- Immediate Actions

# How did we get here?



There are at least six reasons that led us to this point:

- The Economy
- Reduced Revenues
- Added Spending
- State Actions
- Constraints Imposed by the Voters
- The Federal Government

# How did we get here?



## The Economy

### Job Losses

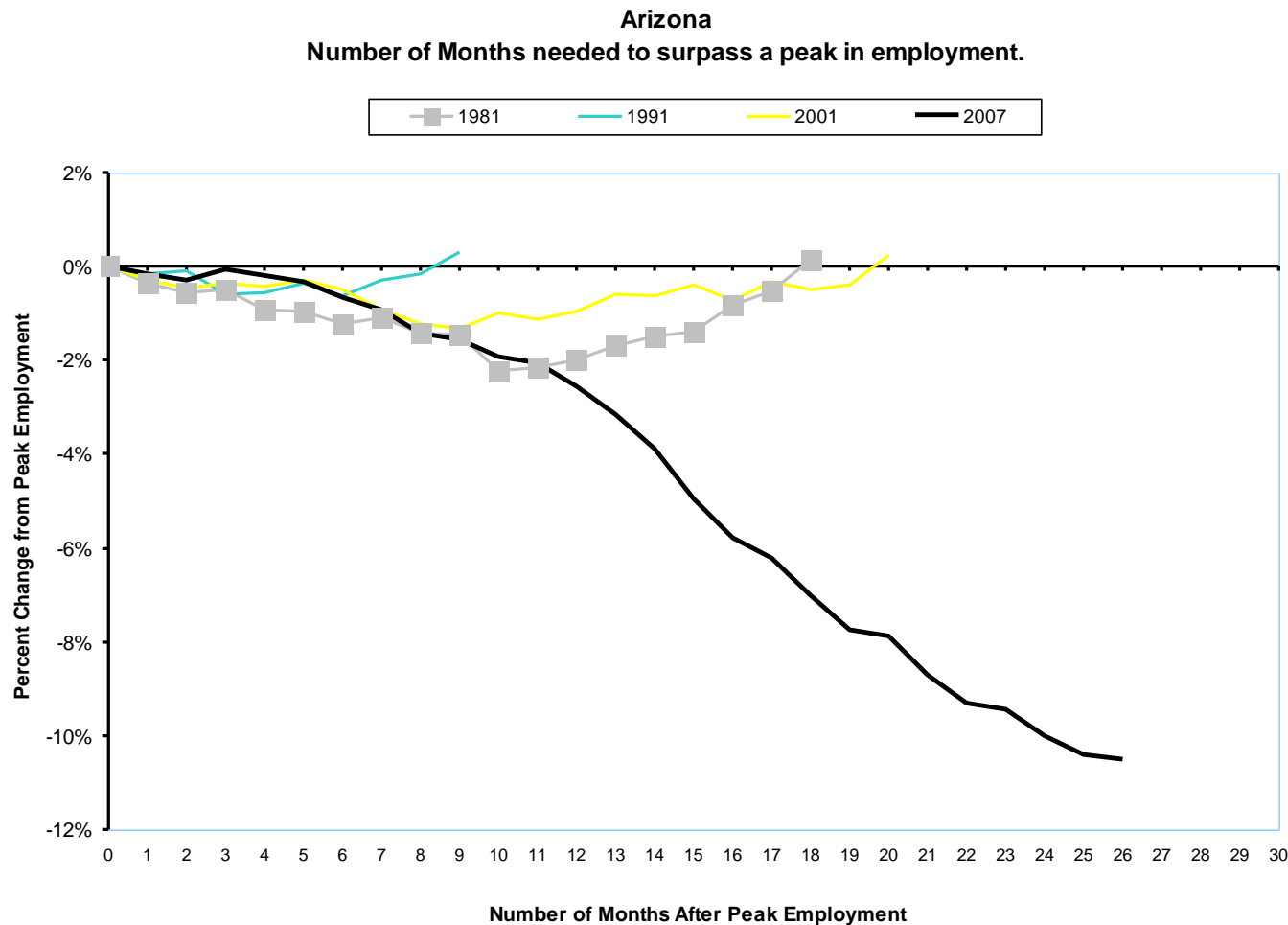
Peak Employment – 2.68 million jobs

– August 2007

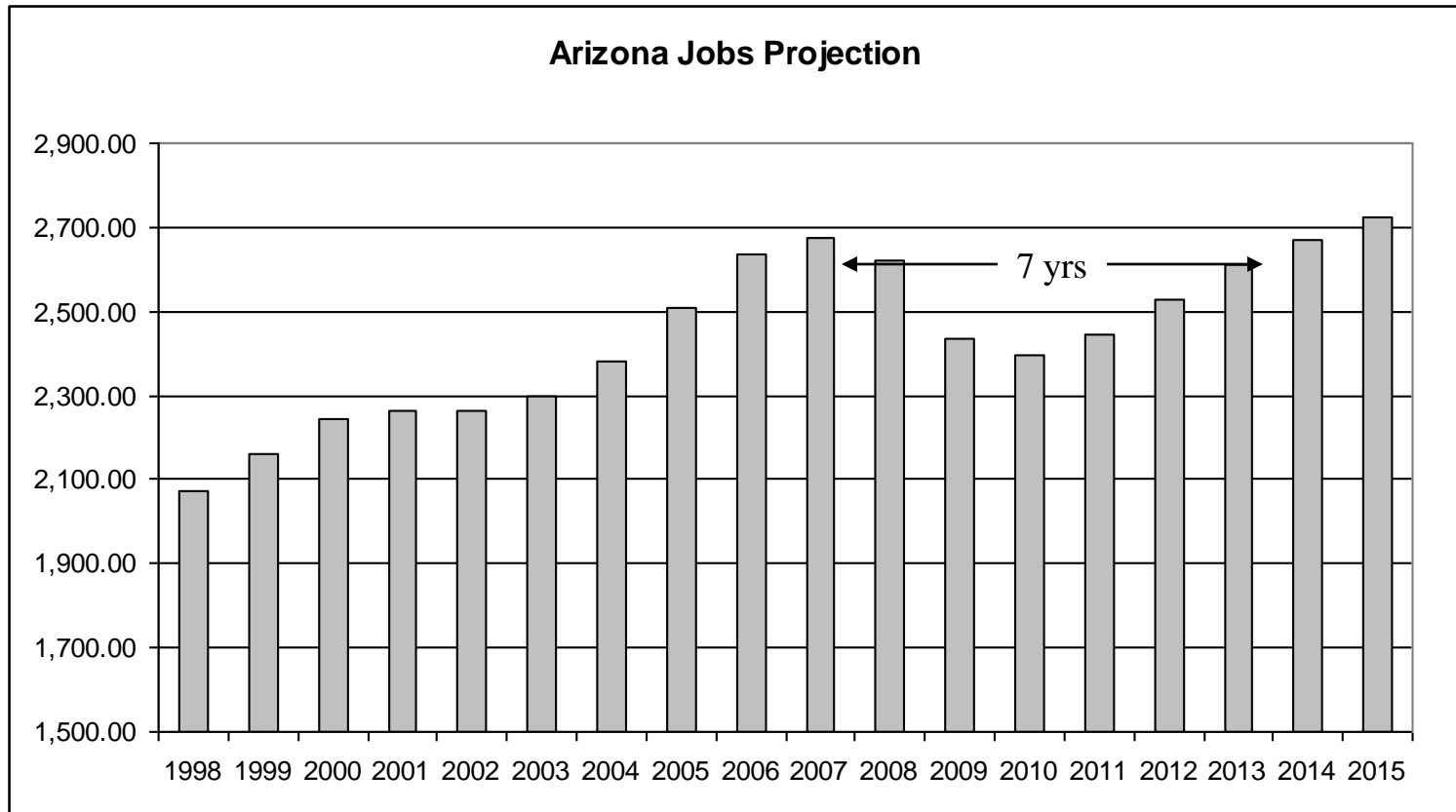
Current Employment – 2.4 million jobs

– Total loss of 280,000 jobs

# How did we get here?



# How did we get here?



Developed by the AZ Department of Commerce

Office of Governor Janice K. Brewer

# How did we get here?



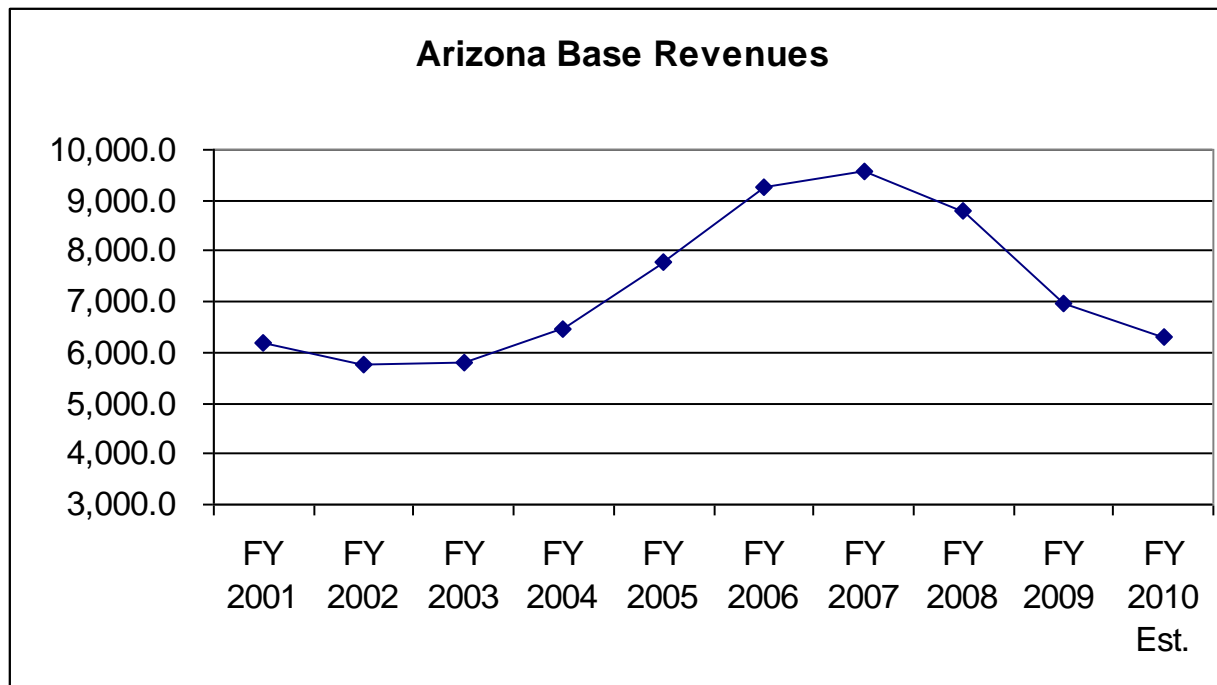
## Reduced Revenues

- Before the recession
  - A series of tax cuts in personal income and corporate income taxes.
- When the recession hit
  - Since FY 2007 Sales (TPT) Tax down 22%
  - Since FY 2007 Personal Income Tax down 38%
  - Since FY 2007 Corporate Income Tax down 57%

# How did we get here?



State tax revenues have declined 34 percent in three years.



# How did we get here?



## Revenue Forecast

- Develop optimistic, baseline, and pessimistic scenarios
- Assume below baseline for both FY 2010 and FY 2011

FY 2010 – 9.4% below FY 2009 actual

FY 2011 – 4.1% above FY 2010 projected (excludes revenue sharing adjustment) – an increase of only \$437.1 million



# How did we get here?



## Growing Populations – Including FY 2011 Estimates

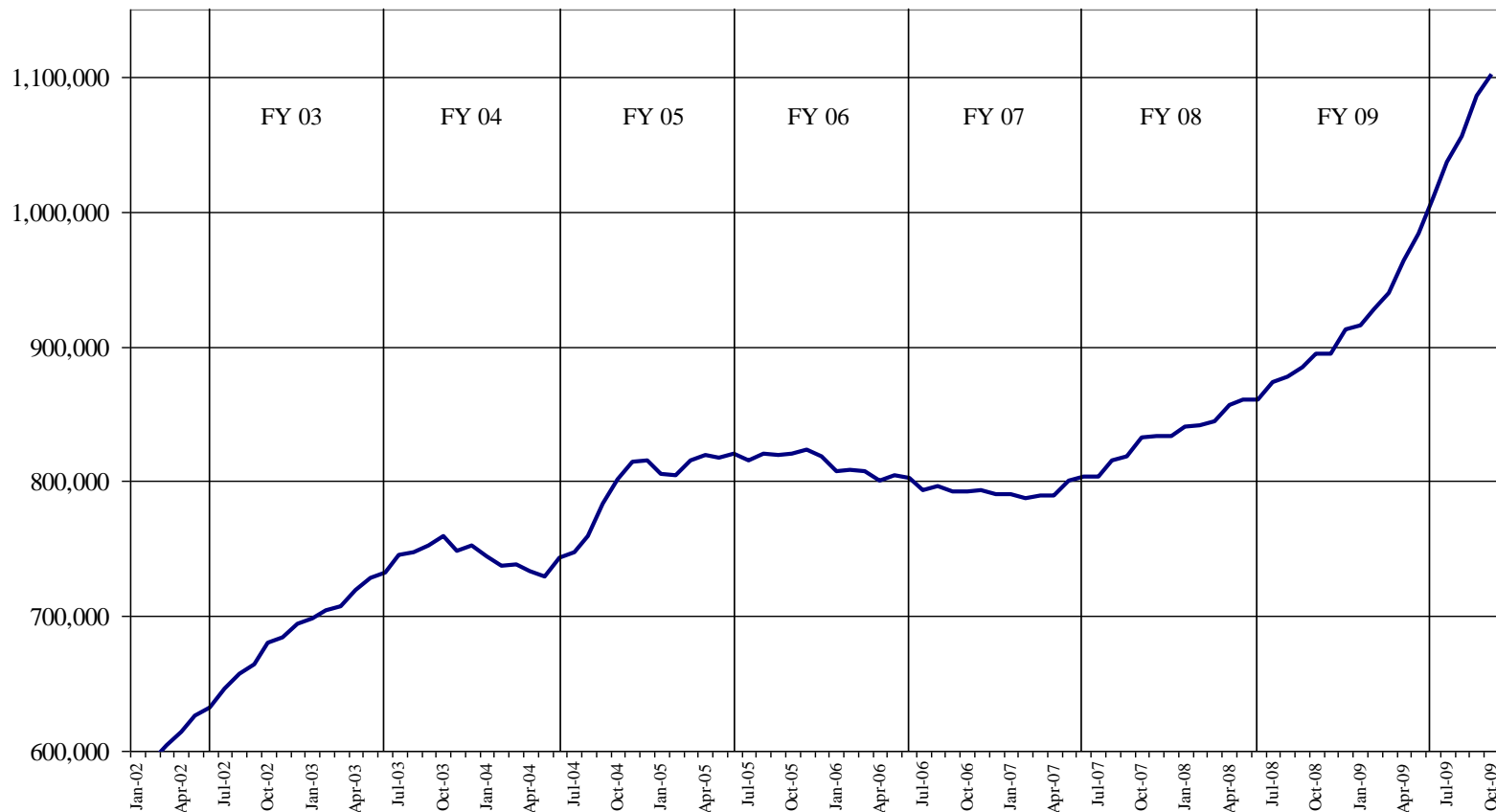
Current revenues = FY 2004

- Since FY 2004, Arizona has added 121,500 K-12 students and more than \$1.0 billion in annual costs to the K-12 system.
- Since FY 2004, enrollment in State universities has increased enrollment by 18,100 students and annual General Fund costs of \$393.5 million.
- Since FY 2004, Corrections has added 10,800 prisoners and annual General Fund costs of \$405.4 million.
- Since FY 2004, AHCCCS has added 475,000 new members and annual costs of nearly \$1.5 billion (General Fund).  
-- In calendar 2009, AHCCCS has grown by 203,000 members --

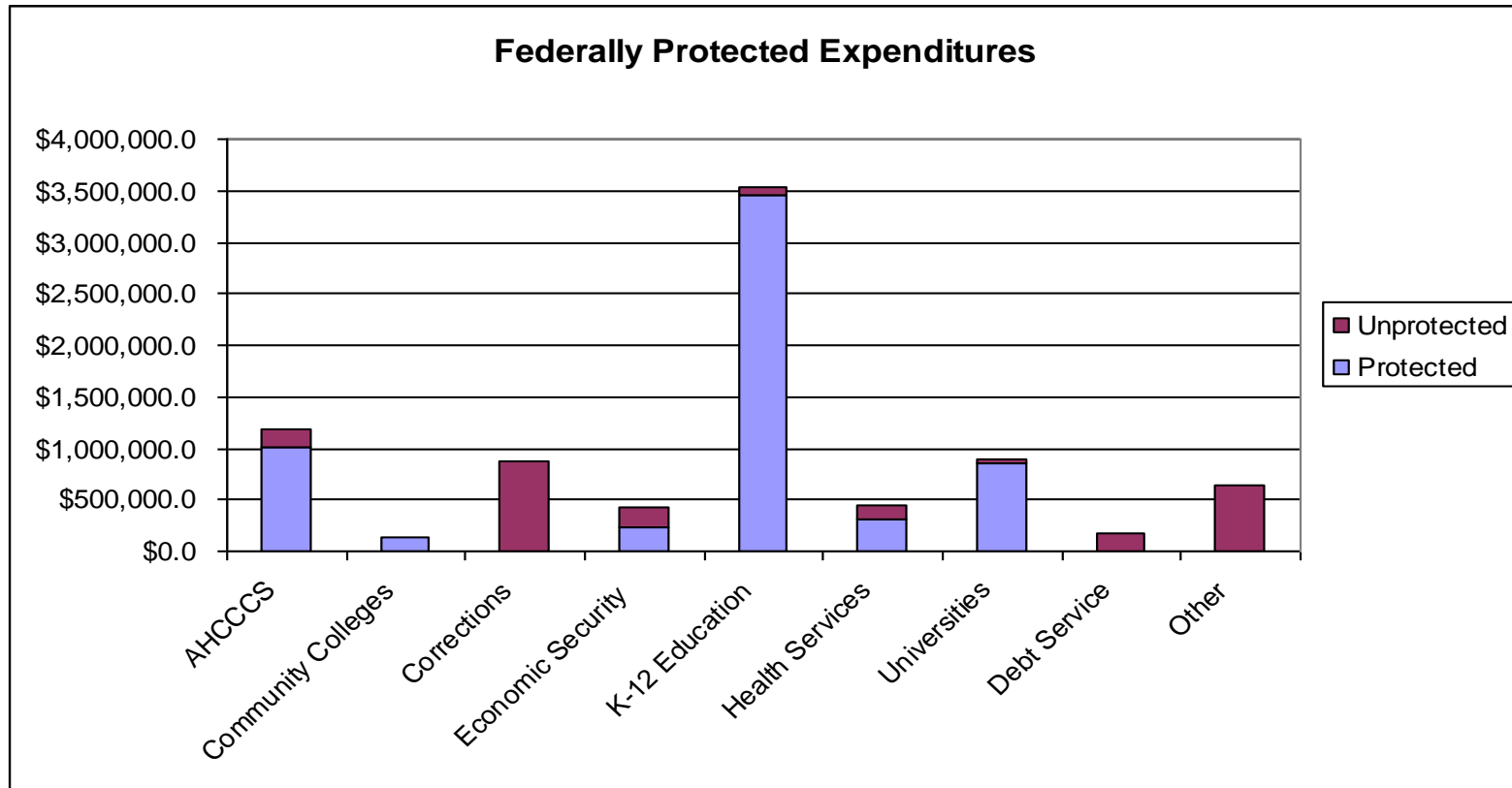
# How did we get here?



**AHCCCS All TXIX Capitation Member Months**



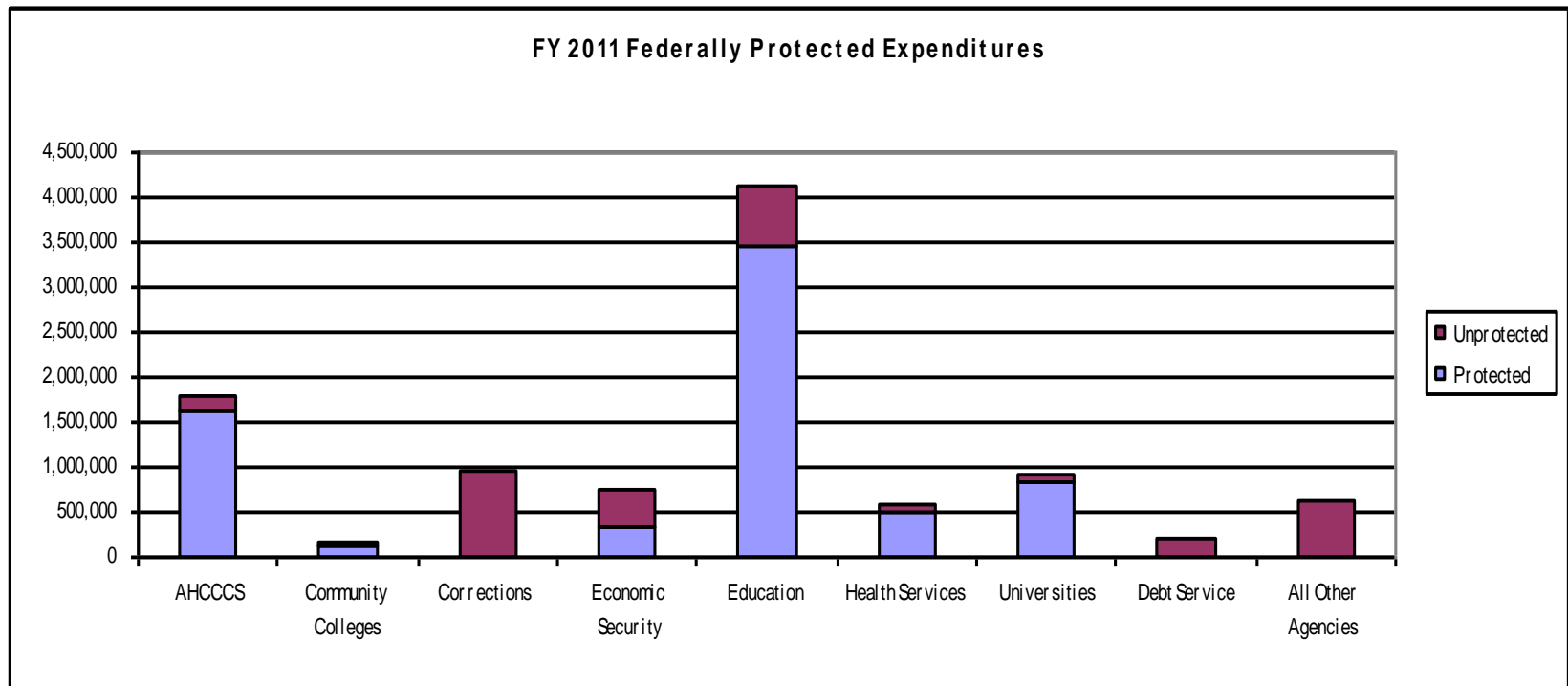
# FY 2010 ARRA MOE Requirements



Approximately \$2.4 billion unprotected

# FY 2011

## ARRA MOE Requirements



Approximately \$3.2 billion unprotected

(Note: Federal MOE for Medicaid currently ends on December 31, 2010)

# How did we get here?



## Major Unprotected General Fund Expenditures

➤ Corrections	\$880 m
➤ Judiciary	\$120 m
➤ Juvenile Corrections	\$68 m
➤ Legislature	\$55 m
➤ Public Safety	\$44 m
➤ Revenue	\$41 m
➤ Kids Care (AHCCCS)	\$30 m
➤ State Only DD (DES)	\$57 m
➤ State Hospital (DHS)	\$65 m
➤ State Only SMI (DHS)	\$79 m

# Summary Budget Status



## FY 2010

- FY 2010 remaining deficit - \$1.4 billion
- FY 2010 remaining unprotected fund - \$1.2 billion

## FY 2011

- FY 2011 deficit - \$3.2 billion
- FY 2011 unprotected funds - \$3.2 billion

## Cash

- External Borrowing of nearly \$1 billion each day to cover cash needs

# Topics



## Budget Status

- What's the Problem?
- How did we get here?

## Budget Recommendations

- **Principles**
- Plan
- Budget Reform
- Immediate Actions

# Principles



“Today marks the most significant day of state budget reform and restructuring in Arizona’s ninety-eight year history. “

- Governor Brewer



# Principles



## Priorities

- Public safety is the core function of State government.
- Education funding is the key to long-term societal and economic development.
- Temporary revenue enhancements should be used only to protect core areas of State government.
- Budget reductions should be strategic and not arbitrary or across-the-board
- Use debt wisely and only as necessary

# Principles



## Strategy

- Attack structural deficit with permanent reforms
- Close deficit for FY 2010 and FY 2011 – no casual deficits
- Use real solutions
- Use temporary steps as necessary
- Quick action to avoid cash shortfalls

# Topics



## Budget Status

- What's the Problem?
- How did we get here?

## Budget Recommendations

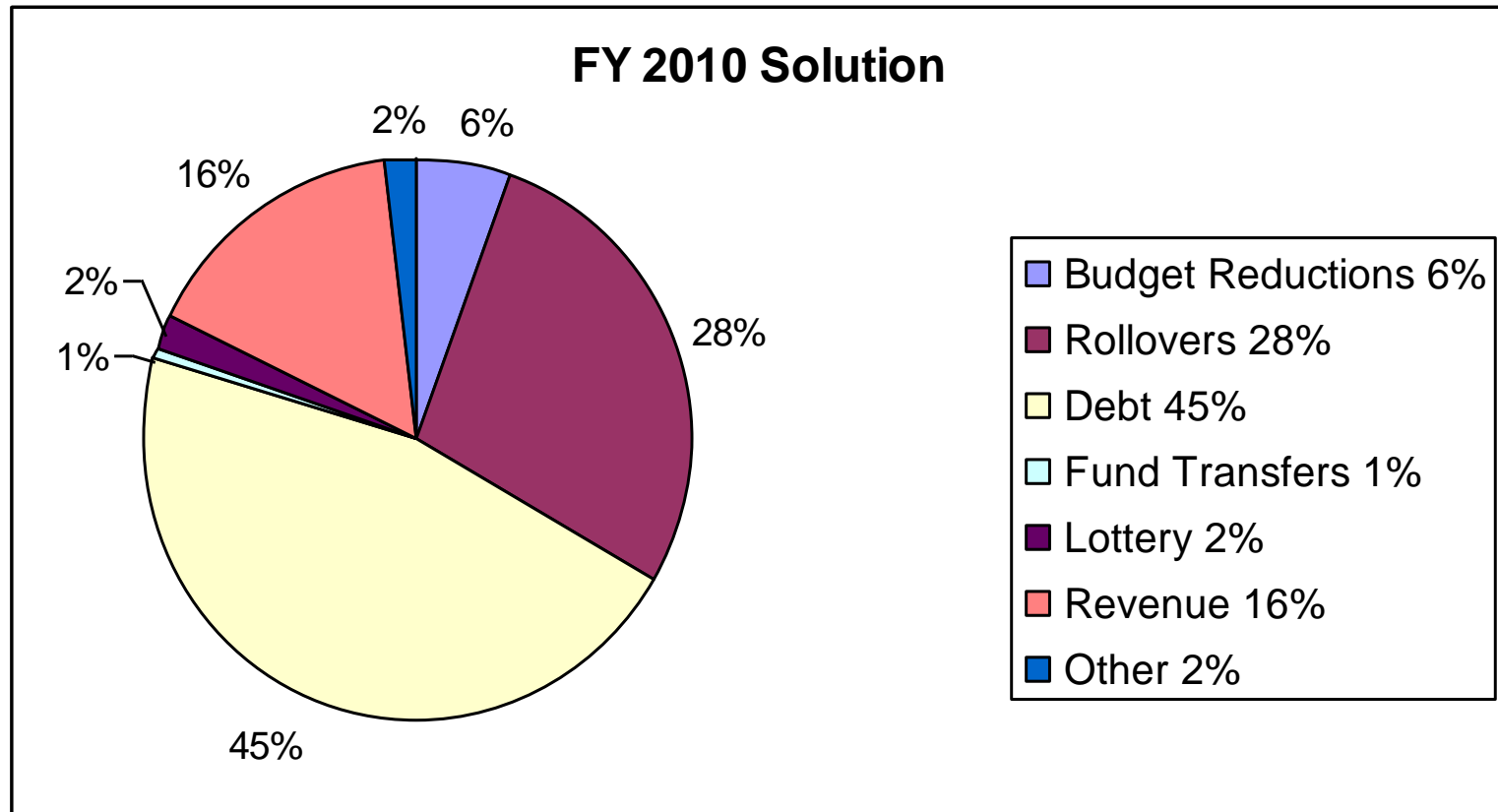
- Principles
- **Plan**
- Budget Reform
- Immediate Actions

# The Plan



- **Overview**
- Public Safety
- Education
- Health and Welfare
- Juvenile Corrections
- General Government
- Revenue

# The Plan – Overview



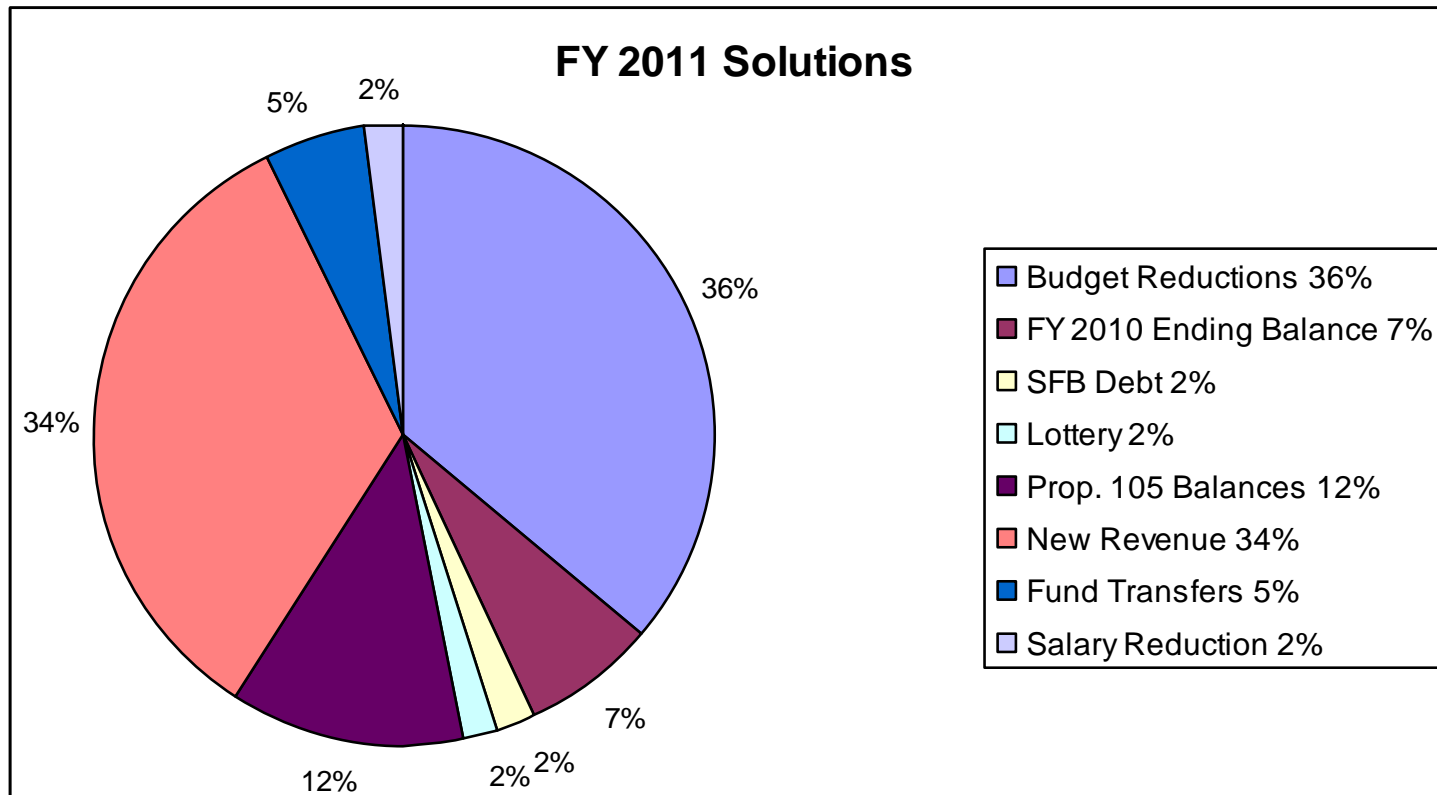
# The Plan – Overview



## FY 2010 Solution

Budget Reductions	6%	\$92.0
Rollovers	28%	\$450.0
Debt	45%	\$750.0
Fund Transfers	1%	\$16.0
Lottery	2%	\$30.0
Revenue	16%	\$263.0
Other	2%	\$26.0
Total		\$1,627.0

# The Plan – Overview



# The Plan – Overview



## FY 2011 Solution

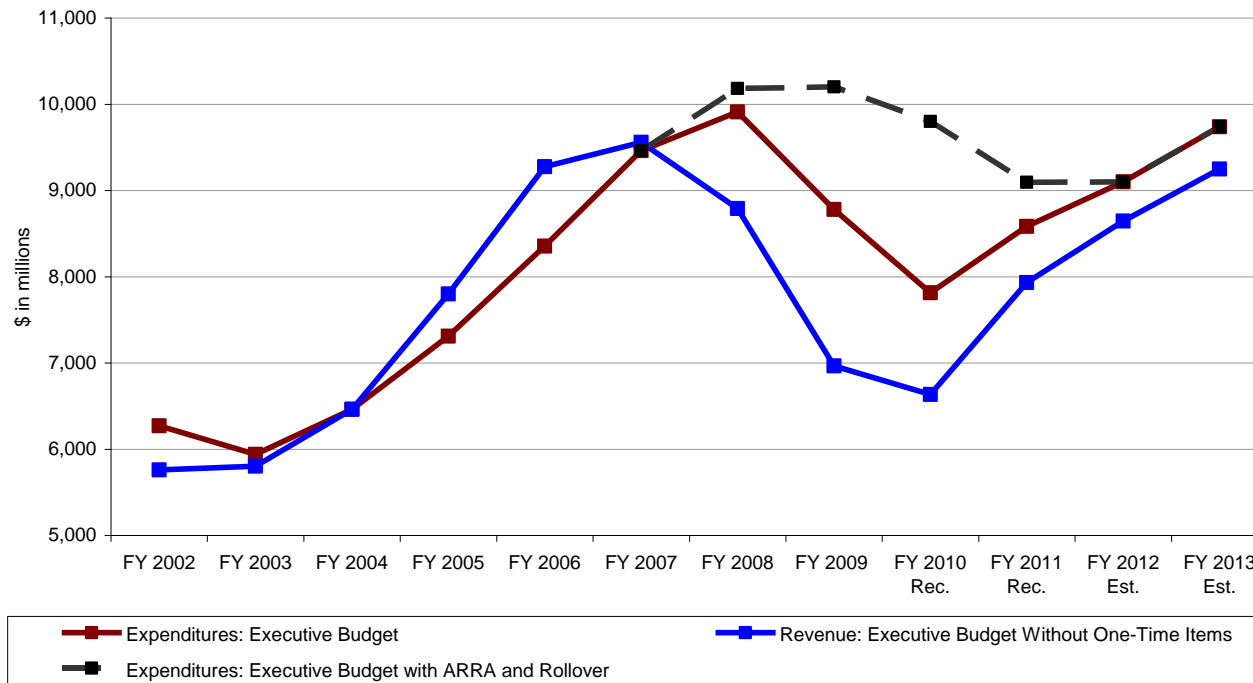
Budget Reductions	36%	\$1,159.0
FY 2010 Ending Balance	7%	\$230.0
SFB Debt Restructure	2%	\$60.0
Lottery	2%	\$60.0
Prop. 105 Balances	12%	\$384.0
New Revenue	34%	\$1,092.0
Fund Transfers	5%	\$173.0
Salary Reduction	2%	\$60.0
Total		\$3,218.0



# The Plan – Overview



The Executive Recommendation



Revenue and expenditures grow after FY 2012 at a projected rate of 7%.

# The Plan – Overview



## FY 2011 Outcome

- GF expenditures: \$8.6 billion
- Including ARRA and Rollovers: \$9.2 billion

Both are between FY 2006 (\$8.3 billion) and FY 2007 (\$9.5 billion) expenditure levels

FY 2011 Ending balance of \$31 million

# The Plan



- Overview
- **Public Safety**
- Education
- Health and Welfare
- Juvenile Corrections
- General Government
- Revenue

# The Plan – Public Safety



\$20 million for local public safety grants

- Funded from the federal stimulus discretionary funds
- Will provide funding for the equivalent 262 positions statewide

Photo Radar – Executive does not intend to renew contract, should be voted on by the people

# The Plan – Public Safety DOC



## Corrections – Bringing Jobs Home

- Eliminating funding for out of state beds (\$86.5 million)
- Funding for 2,000 private in state beds \$40 million
- New 4,000 public in state beds \$58.4 million
- Backfill stimulus funds \$50 million
- Backfill medical funds \$20 million

# The Plan – Public Safety DOC



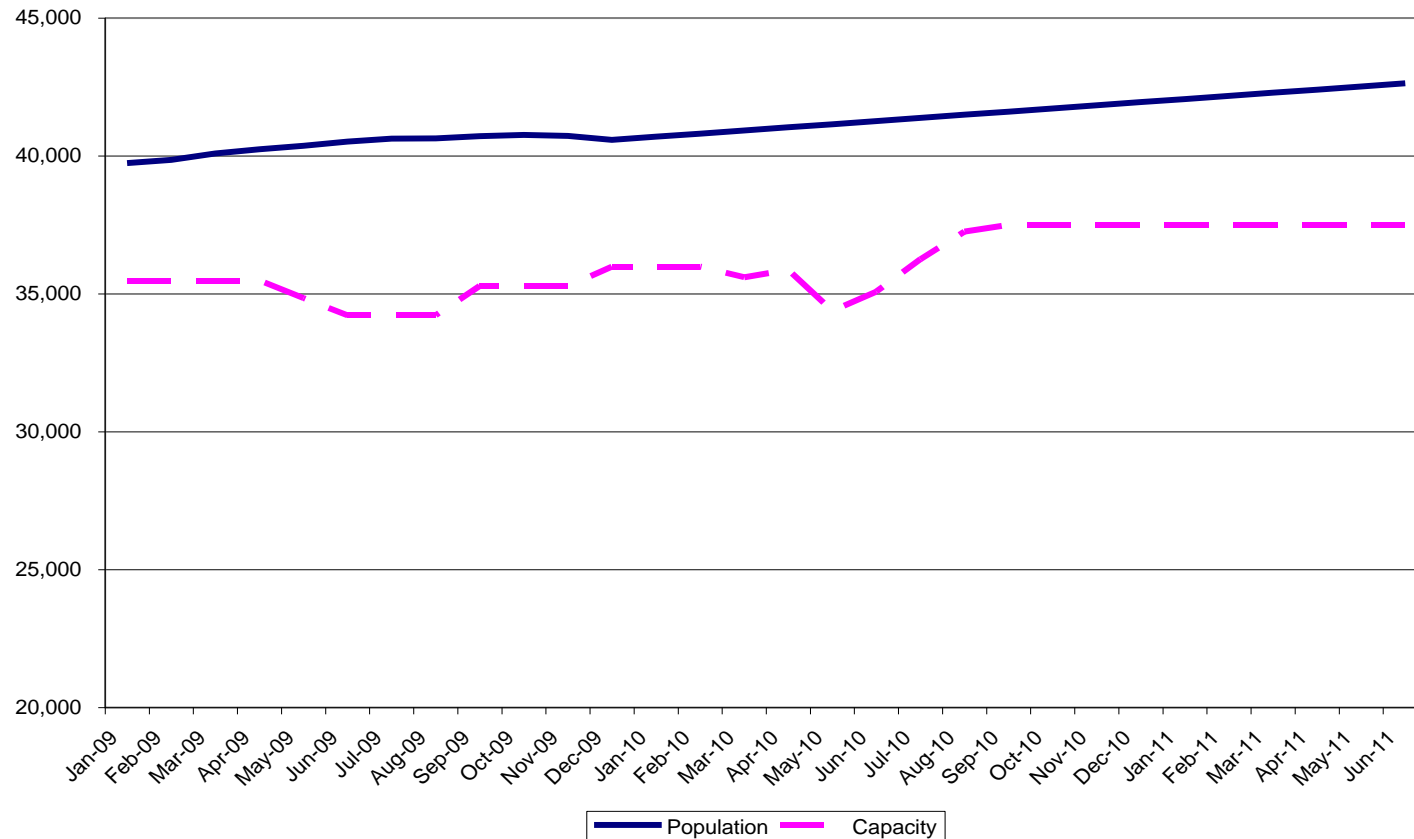
## Expected Growth

- The Executive budget estimates population growth to be 114 inmates per month or 1,368 per year
- New beds will be needed in FY 2013 and FY 2014
- End FY 2011 with a bed deficit of 5,135

# The Plan – Public Safety DOC



Inmate Population Growth Compared to Capacity



# The Plan



- Overview
- Public Safety
- **Education**
- Health and Welfare
- Juvenile Corrections
- General Government
- Revenue



# The Plan – K-12 Education



## FY 2010 – Eliminate funding for non-formula programs

- AIMS Intervention
- Adult Education and GED
- Chemical Abuse
- Gifted Support
- Early Education Block Grant
- Vocational Education Block Grant
- Teacher Training

# The Plan – K-12 Education



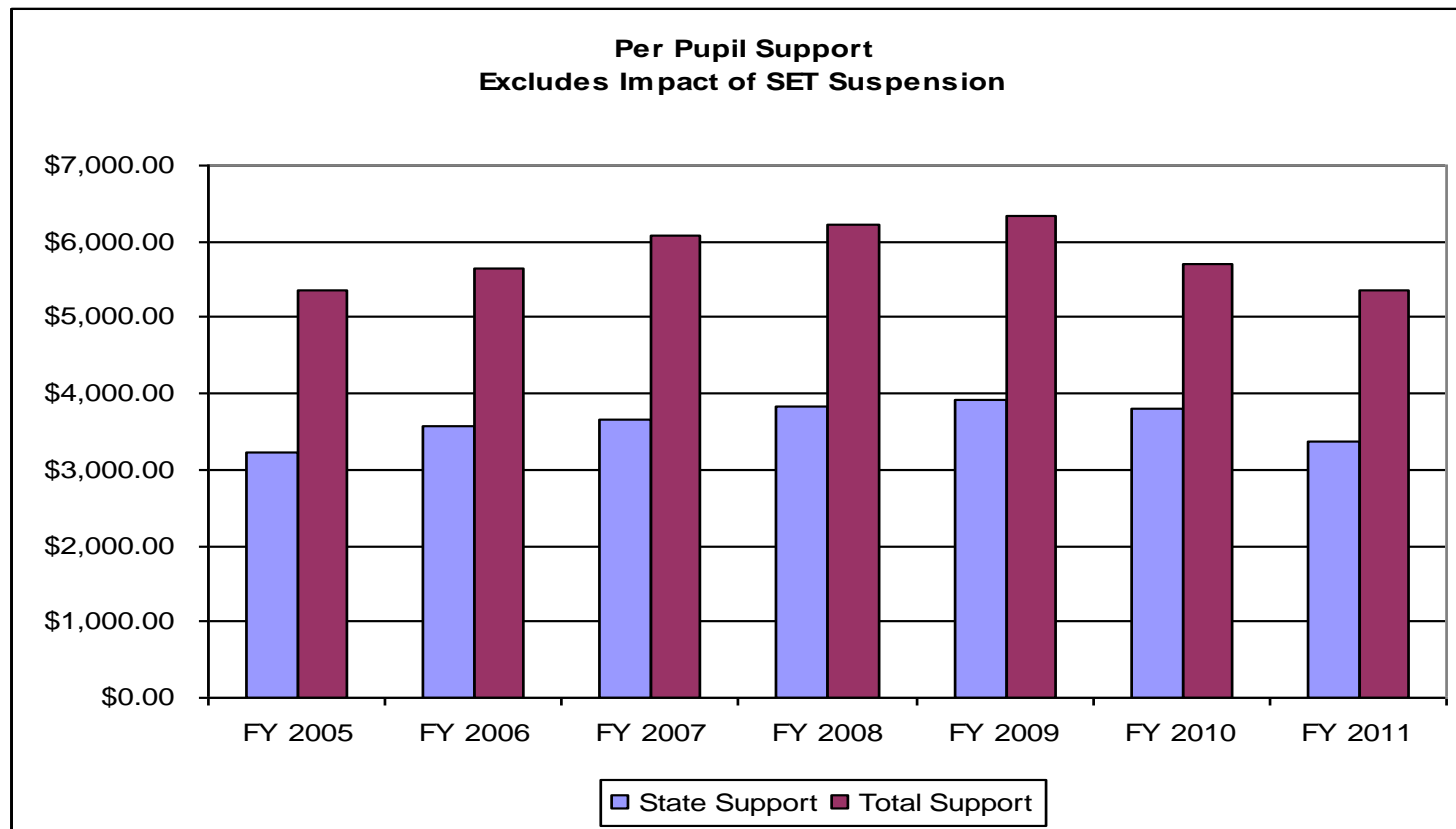
## Protect Funding at FY 2006 Levels

- Eliminate kindergarten funding weight (\$218 million)
- Reduce Charter Additional Assistance (\$10 million)
- Reduce Early Graduation (\$5 million)

# The Plan – K-12 Education



Per pupil support for FY 2011 falls between FY 2005 and FY 2006 levels



# The Plan – K-12 Education



## School Facilities Board

### New Construction

- 92 school districts still growing
  - West side of Phoenix
  - Outskirts of Tucson
- Legislature provided \$100 million for new schools financed through a federal bonding program
  - Requires supplemental interest
  - Subject to federal construction law

**Recommendation – Use the best financing for the State**

# The Plan – K-12 Education



## School Facilities Board

### Building Renewal

- Approximately 120 million square feet of academic space
- No funding for building renewal formula

### Recommendation

- \$5 million for building renewal grant funds for most critical projects

# The Plan – Higher Education



## Universities

- Maintain support at FY 2006 levels
- Reduces per pupil support to \$7,100 per pupil (FY 2008 level was \$9,480)

## Community Colleges

- Maintain support at FY 2006 levels

# The Plan - Education



## Rollovers

K-12                      \$350 million (May payment)

Universities        \$100 million

Total Rollovers at end of FY 2010 = \$1.3 billion

# The Plan



- Overview
- Public Safety
- Education
- **Health and Welfare**
- Juvenile Corrections
- General Government
- Revenue



# The Plan – Health and Welfare



## AHCCCS Baseline

- Medicaid Population Growth \$389 million
- Federal Stimulus Backfill \$202 million

# The Plan – Health and Welfare



## Proposition 204

- Expanded Medicaid coverage to all populations under 100 percent of federal poverty limit (Approx. \$22,000 for family of four) including childless adults
- FY 2011 cost of the expansion

Tobacco	\$173.3 million
General Fund	\$744.7 million

Note: numbers exclude ARRA

# The Plan – Health and Welfare



## Proposition 204

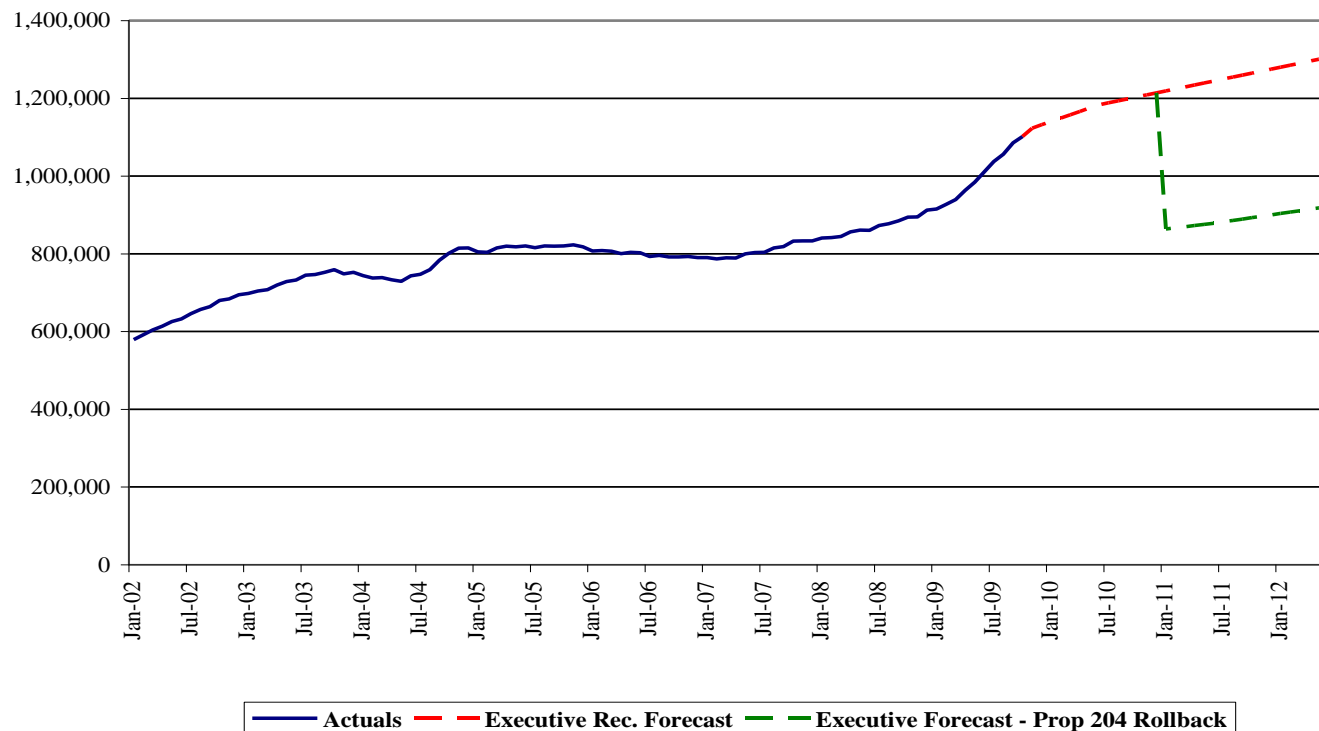
The Executive proposes holding a special election and amending the federal waiver to eliminate General Fund support for this program as of January 1, 2011.

- Eliminate support for childless adults
  - Cap other populations at the support level covered by the Tobacco Settlement
- 
- An estimated 310,500 people will lose coverage
  - State will lose \$737.6 million in Federal matching funds
  - GF will save \$382.5 million in FY 2011, \$1 billion in FY 2012

# The Plan – Health and Welfare



**AHCCCS TXIX Capitation Member Months  
Actuals and Forecasts**



Approximately 25 percent of the current Medicaid population will lose services.

# The Plan – Health and Welfare



## Potential Federal Impacts

### Extension of MOE with enhanced FMAP

- Net gain in FY 2011 of \$41.5 million
- FY 2012 funding cliff of nearly \$1 billion

### Health Care Reform

- Eliminate savings
- Will increase costs by \$400 million per year in FY 2014

# The Plan – Health and Welfare



## Other AHCCCS Issues (all receiving 2:1 or 3:1 federal match)

- The Executive recommends eliminating the KidsCare program, saving \$22.9 million. KidsCare provides health coverage for 46,800 children with incomes below 200% of FPL.
- Capitation rate growth held flat; will likely result in provider rate reductions, saving \$57.1 million.
- Optional benefits are eliminated under the Executive proposal for a \$6.3 million savings.
- The Executive proposes eliminating GME and DSH hospital subsidies, leaving a \$500,000 total fund minimal DSH program.

# The Plan – Health and Welfare



## Department of Health Services

### Baseline Adjustments

Medicaid Behavioral Health Caseload, ARRA Backfill, and Inflation

- \$25.4 million in FY 2010
- \$146.6 million in FY 2011

Medicaid Children Rehabilitative Services Caseload, ARRA Backfill, and Inflation

- \$5.4 million in FY 2010
- \$13.1 million in FY 2011

# The Plan – Health and Welfare



## Arnold v. Sarn

- Change the statute that requires funding for Arnold v. Sarn, Non-TXIX SMI, and the Court Monitor
  - 17,400 Adults impacted
  - Saves \$37 million



# The Plan – Health and Welfare



## Arnold v. Sarn Elimination

- Preserves \$21 million for new stand-alone Crisis Intervention and Supported Housing
- Preserves \$37 million to fund medications for all Non-TXIX SMIs

# The Plan – Health and Welfare



## Other DHS Issues

- Capitation Rate Adjustments
  - (\$5.0 million) in FY 2010
  - (\$22.0 million) in FY 2011
- Risk Sharing Adjustments
  - (\$10.0 million) in FY 2010
  - (\$6.2 million) in FY 2011
- BHS Reform
  - Transfers TXIX General Mental Health and Substance Abuse clients to AHCCCS
  - Creates a Pilot Program to integrate SMI services at AHCCCS
- ASH Funding
  - Counties will now pay full cost of housing SVPs at the State Hospital. They currently only pay 25%.

# The Plan – Health and Welfare



## Department of Economic Security

### Baseline Issues

#### TXIX Caseload and Inflation

- \$28.5 million GF in FY 2011
- Includes funding for the Developmentally Disabled

#### ARRA Backfill

- \$101.3 million GF in FY 2011
- Backfills loss of enhanced FMAP, State Fiscal Stabilization Dollars, and other funding available in ARRA

#### TANF Shortfall

- \$30.3 million in FY 2010
- Childcare TANF appropriation reduced
- \$58.9 million in FY 2011
- Annualizes Childcare Savings and Cash Assistance Savings; backfills a portion of the GF shortfall

# The Plan – Health and Welfare



## Program Eliminations (FY 2010)

- Sight Conservation
- DD Provider Enhanced Rates
- Grandparent Kinship Care
- SSBG Planning Funds for local governments

## Means Testing

- Means test all members of household for Cash Assistance Benefits
- Increase Child Support Clearinghouse Fee from \$2.25 per payment to \$5.00 per payment
- Increase amount billed to SSI for DD Services
- Bill adoption subsidies for families that place adoptive child in a residential home
- No longer exceed cost-effectiveness limit of \$138,500 per year for DD clients in the community
- Eliminate DD services to families that refuse to provide billing information

# The Plan – Health and Welfare



## Cash Assistance Restriction (FY 2010)

- Reduces benefit from 60 months to 36 months
- Eliminates services for approximately 10,000 families
- Recommended for implementation April 1, 2010

# The Plan



- Overview
- Public Safety
- Education
- Health and Welfare
- **Juvenile Corrections**
- General Government
- Revenue

# The Plan – DJC



## Department of Juvenile Corrections

- The Executive recommends closing DJC and shifting responsibility for this population to the counties
  - The 1996 Juvenile Justice Act changed the type of juvenile being placed with DJC
  - Current population is largely composed of juveniles with substance abuse and property offenses
  - DJC population has declined

# The Plan – DJC



## DJC Populations

<u>Fiscal Year</u>	<u>Average Daily Population</u>	<u>Funding</u>	<u>Per Capita</u>
2005	618	\$72,132,000	\$116,718
2006	617	\$76,048,100	\$123,255
2007	593	\$84,266,800	\$142,103
2008	603	\$85,920,700	\$142,489
2009	595	\$82,370,400	\$138,438
2010	494	\$70,622,500	\$143,067



# The Plan – DJC



## DJC (cont'd)

- Rehabilitation and treatment is more successful when families and support systems are involved
  - Keeping youth close to home will make it easier for families to participate
  - Nationally, states are shifting to a model of regionalization where juveniles are treated closer to home
- Many redundancies exist in the juvenile justice system
- Most counties have the capacity to treat juveniles from their counties
- Commission will be put in place to oversee transition

# The Plan



- Overview
- Public Safety
- Education
- Health and Welfare
- Juvenile Corrections
- **General Government**
- Revenue

# The Plan – General Government



## State Parks

- The Parks Board is voting this week on closing 21 of 30 state parks

## Executive Budget Recommendations

- Continue use of session law to allow spending for operations out of other agency funds
- Fold all special line item expenditures into lump sum
- Cancel unspent grants from Heritage Fund in FY 10
- Take operational reductions from grant programs as much as possible instead of parks

# The Plan – General Government



## The Executive recommends

- Funding COP balloon (\$14.3 million)
- Funding basic building renewal (\$20 million)
- Reducing state employee pay (5 percent)
- Eliminating Growing Smarter payments and sweeping the Land Conservation Fund (\$124 million)
- Redirecting Lottery Revenues to the General Fund
- Moving ADEQ, Water, Tourism to self funding

# The Plan – General Government



## Debt Recommendations

### FY 2010

- Bonds from lottery revenue streams \$450 million
- Expand sale/leaseback transaction \$300 million

Increases annual debt service payment by an estimated \$45 million.

Total new FY 2010 debt is \$1.585 billion. Estimate FY 2011 debt service of \$87 million

### FY 2011

- Refinance SFB debt \$60 million
- Borrow funds from First Things First \$260 million

# The Plan – General Government



## Debt

### Sale/Leaseback Summary

- Original issue amount \$735 million
- Sold on January 12 and 13
- Over \$1 billion in orders
- 4.57 percent interest over 20 years
- Annual debt service payment of

# The Plan – General Government



## Impacts on Local Government

- Shift of DJC population
- Shift of Lottery funds
- Shift of Tourism funds
- Eliminate County Hold Harmless
- Charge counties for ASH costs
- Eliminate SSBG planning funds
- Eliminate County Attorney Immigration Enforcement

# The Plan - Summary



## FY 2010 – Reductions \$92 million

➤ Salary Reduction	\$15 million
➤ K-12 Non Formula	\$28 million
➤ Reduce Cash Assistance	\$ 9 million
➤ Other DES	\$14 million
➤ Arnold v. Sarn	\$15 million
➤ County ASH Payments	\$ 7 million
➤ Other	\$ 4 million



# The Plan



- Overview
- Public Safety
- Education
- Health and Welfare
- Juvenile Corrections
- General Government
- **Revenue**

# The Plan – Revenue



## Revenue Enhancements

Item	FY 2010	FY 2011
One Cent Increase in TPT	202,000.0	898,000.0
Expanding TPT tax base to repairs	13,000.0	156,200.0
Lowering the threshold on TPT estimated payments	48,000.0	
Repealing the TPT accounting credit		20,000.0
<b>Total</b>	<b>263,000.0</b>	<b>1,074,200.0</b>

Represents a 14.3 percent increase in base revenues

# The Plan – Revenue



## Department of Revenue Collection Enhancement

Item	Value
Restore Audit Staff	\$1,798.0
Increase Collectors	\$1,195.0
Statutory Changes	\$14,871.8
Total	\$17,864.80

# Topics



## Budget Status

- What's the Problem?
- How did we get here?

## Budget Recommendations

- Principles
- Plan
- **Budget Reform**
- Immediate Actions

# Budget Reform



## Constitutional Balanced Budget Provision

## Constitutional Budget Stabilization Fund

- Current cap of 7 percent is too small
- Legislature has history of suspending the requirements for using the fund
- Requirements to place excess revenues in the fund will serve as an expenditure limit
- Constitutional limits on accessing the fund will preserve fund to help buffer economic downturns

## Prop 105 Reform

- Allow Legislators under specific circumstances to modify provisions of voter-approved programs

# Budget Reform



## Executive Authority to Reduce Appropriations

- In over 20 other states, the Executive has some form of authority to reduce appropriations
- The Governor should have authority under certain conditions to modify appropriations – including voter-approved programs

# Budget Reform



## State Fee Commission

Ensure appropriate use of state-charged fees

- Build a comprehensive list of all fees levied
- Determine actual cost of services provided regardless of fund source
- Recommend periodic adjustment to fee levels from external (e.g. inflation) or internal (e.g. caseload) causes

# Topics



## Budget Status

- What's the Problem?
- How did we get here?

## Budget Recommendations

- Principles
- Plan
- Budget Reform
- **Immediate Actions**



# Immediate Actions



To implement the plan, the Legislature must take immediate action on the following proposals:

1. New revenues
2. Debt package, including the Lottery extension
3. Closing DJC
4. Rollovers
5. 5 percent pay reduction
6. Reform cash assistance
7. Reform Arnold v. Sarn
8. Referral package for May special election